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IN THE

Supreme Court of the United States

October Term, 1941

No. 806

315-801

PAUL E. MANHEIM, as a Committee, and THE CHASE NATIONAL BANK OF THE CITY OF NEW YORK, as Trustee,
Petitioners,

against

VAN S. MERLE-SMITH, *et al.*, J. P. MORGAN, *et al.* and J. HERBERT CASE, *et al.*, Contracting Committees, The City of New York, the Transit Commission and all other parties to Plan and Agreement to end the receivership of Interborough and Manhattan Companies, Thomas E. Murray, as Interborough Receiver, and William Roberts, Receiver of Manhattan Railway Company,
Respondents.

Petition for Writ of Certiorari to the United States Circuit Court of Appeals for the Second Circuit (Including Brief in Support Thereof)

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Respondents.

Petition for Writ of Certiorari to the United States Circuit Court of Appeals for the Second Circuit (Including Brief in Support Thereof)

Paul E. Manheim as an owner of and as attorney-in-fact for other owners of Manhattan Railway Company 4% Second Mortgage Bonds in the aggregate principal amount of $484,000, prays for a writ of certiorari to review the order (R. 968) of the United States Circuit Court of Appeals for the Second Circuit, entered on September 23, 1941, pursuant to the decision of that Court (SWAN, AUGUSTUS N. HAND and CLARK, JJ.) affirming without costs various orders and decrees (R. 187-272, 287-9, 318, 410-9, 455-561, 566-575) of the United States District Court for the Southern District of New York made herein on December 11, 1939 and on March 4, March 15, June 10,

June 12, and October 30, 1940. The Chase National Bank of the City of New York, as Trustee for the Manhattan 4% Second Mortgage Bonds, joins in this petition to the extent indicated at the end hereof.

Opinions Below.

The opinion of the District Court for the Southern District of New York (R. 400-409) is unreported. The opinion of the Circuit Court of Appeals for the Second Circuit (R. 951-62) is reported in 122 F. (2d) 454.

Jurisdiction.

The jurisdiction to issue the writ requested is found in the provisions of Sec. 240(a) of the Judicial Code as amended by the Act of February 13, 1925 (c. 229, Sec. 1, 43 Stat. 938; 28 U. S. C. A. Sec. 347(a)). This Court has already passed on the jurisdiction of the District Court over the receivership out of which this case arose in *Johnson* v. *Manhattan Ry. Co.*, 289 U. S. 479, at page 487.

Statutes Involved.

No statute is involved here but there is involved a construction of paragraphs "(a)" and "(c)" of Rule 23 of the Federal Rules of Civil Procedure.

The Questions Presented.

This controversy arises out of the treatment of non-assenting Manhattan 4% Second Mortgage Bonds under the consummation of the Unification Plan pursuant to which two jointly operated transit companies in Federal equity receivership, Manhattan Railway Company (hereinafter called "Manhattan") and Interborough Rapid Transit Company (hereinafter called "Interborough"), were liquidated and the City of New York acquired their prop-

erties for City operation. The Plan provided that the City would pay for the properties of both companies a single price of $164,000,000, consisting of about $20,000,000 in cash and $144,000,000, in principal amount of New York City 3% Corporate Stock* of a type then selling around par. Security holders of each company who assented to the Plan agreed to take for their securities the Plan prices, that is payments out of the $164,000,000 made largely in Corporate Stock, in amounts specified in the Plan and fixed as a result of negotiations between groups of security holders. Security holders who did not assent to the Plan within three months of its consummation (R. 94-9), such as the petitioner and those he represents, were to receive "the cash distributive share to which all holders of securities shall be legally entitled" (R. 102), the amounts of which were not fixed in the Plan. The cash distributive share of non-assenting Manhattan Second Mortgage Bonds has been fixed at $394.68 per Bond (R. 566-9) by means of a foreclosure sale designed to show that this issue had no rights in the Manhattan physical assets and a class action supposed to fix its rights in the remaining assets, the claims of Manhattan parties against Interborough. The general question presented is whether the legal cash distributive share of non-assenting owners of Manhattan Second Mortgage Bonds has been properly fixed at $394.68 per Bond.

The problem before the courts in determining the petitioner's legal cash distributive share would appear to have been one of valuing the municipal bonds forming part of the $164,000,000 fund and thereafter determining rights in that fund. This has never been done, but, instead, the reorganization technique of fixing all legal cash distributive shares so low that all will assent has been misapplied here to a liquidation proceeding. Where it is necessary to coerce people into taking securities in a reorganized

* Corporate Stock is one form of New York City bonds. For prices at which it has sold, see page 11 hereof.

enterprise, in lieu of cash, in order to retain enough cash to run the enterprise, this reorganization technique may be justified on the ground of necessity; but on the liquidation of a corporation by the sale of its assets to an outside purchaser, the purchaser alone has the responsibility of obtaining the cash to run the enterprise and the reorganization technique of coercive judicial sales has no place, be the purchase price paid in cash, coal or municipal bonds.

The petitioner has ventured the foregoing remarks because his petition loses much of its point should the Court fail to realize at the outset that this case involves a liquidation, not a reorganization.

More specifically, the questions presented are:

I. Whether any compromise of a class action brought to determine the legal cash distributive share of non-assenting holders of Manhattan 4% Second Mortgage Bonds (and only of non-assenting holders of this issue) on the liquidation of their corporation, should have been approved by the District Court under Rule 23(c) of the Federal Rules of Civil Procedure, when the compromise was not agreed to by any non-assenting Manhattan Second Mortgage Bondholder or by any representative of such a Bondholder and was opposed by the petitioner.

II. Whether a compromise of a class action should have been approved by the District Court under Rule 23(c) which fixes at $394.68 per Bond the legal cash distributive share of non-assenting holders of Manhattan 4% Second Mortgage Bonds (in the principal amount of $1,000 each and on which no interest has been paid since December 1, 1933, R. 154) on the liquidation of their corporation, on the apparent basis of determinations:

(a) that the properties of both companies bought by the City for cash and municipal bonds worth about

$164,000,000 were sold on the same day by the companies for but $97,000,000 in cash;

(b) that the legal cash distributive shares of all Manhattan security holders in the $97,000,000 totaled but $41,000,000, although the Interborough parties, none of whom appealed, permitted the Manhattan parties to take some $51,000,000 ($16,500,000 in cash and $34,500,000 in that principal amount of municipal bonds worth about par) out of the $164,000,000; and

(c) that the Manhattan stockholders were entitled to over $9,500,000 out of the $41,000,000* as a result of their disputed and undecided contention that they had a direct claim as creditors of Interborough for an undetermined amount.

III. Whether a compromise of a class action should have been approved by the District Court under Rule 23(c) which fixes at $394.68 per Bond the legal cash distributive share of non-assenting Manhattan 4% Second Mortgage Bonds on the liquidation of their corporation, where the $394.68 was actually fixed by taking 80% of the $500 Plan price (R. 888-91), a price determined in negotiations in which the only representatives of any Manhattan Second Mortgage Bonds indicated that they did not represent the issue as a whole (R. 316, 581, 593, 91, 146).

IV. Whether, if the $394.68 per Bond has not been properly fixed, the Manhattan Second Mortgage Bondholders are entitled on this Record to be paid in full or to the Plan price of $500 in Corporate Stock or to a new trial.

No question is presented (a) which might require the City to return the transit properties to the companies or

*$41,000,000 would have been enough to pay principal and interest in full to all non-assenting Manhattan bondholders of both issues and to pay the assenting Manhattan bondholders of both issues the Plan prices which they had agreed to take by assenting (see table at page 12 hereof and R. 403, 409).

affect those security holders who assented to the Plan, or (b) as to the right of Manhattan to sell its properties to the City, together with the properties of Interborough, for a single sum payable partly in municipal bonds, or (c) as to the amount of the purchase price.

Statement.

(a) Relationship between Manhattan and Interborough

In 1903 Manhattan leased all its then existing properties for 999 years to Interborough, and Interborough operated these properties (elevated railroads and a power plant) since that time until their recent acquisition by the City of New York for operation by it. Under the Lease (Exhibit 4, Vol. III) Interborough agreed, among other things, to pay Manhattan, as rent, taxes on Manhattan properties, interest on bonds outstanding and to be issued, and $7 a share per annum for each of the 600,000 shares of Manhattan stock of the par value of $100 per share then outstanding or shortly to be issued. The Lease gave Interborough the privilege of paying directly to the Manhattan stockholders their annual payment after Manhattan had declared a dividend (see Exhibit A annexed hereto). Interborough endorsed on the Manhattan stock certificates a guaranty to pay in accordance with the Lease. The Lease made no provision for paying principal on Manhattan bonds then outstanding in the principal amount of almost $40,000,000 (Exhibit 4, p. 12). In 1922, most of the Manhattan stockholders agreed to a reduction in the annual payment to them to $5 per share per annum, payable only if earned by Manhattan or Interborough (R. 154, 809-11, Exhibit 14, Vol. IV).

(b) The Securities Owned or Represented by the Petitioner

Manhattan had outstanding on the date of consummation of the Plan of Unification, an issue of Consolidated Mortgage Bonds in the principal amount of $40,670,000 ahead of the Second Mortgage Bonds (R. 154). The petitioner and

those he represents as attorney-in-fact own $484,000 in principal amount of the Second Mortgage Bonds (R. 897, 954) or over 10% of an issue of but $4,523,000 in principal amount (R. 154).

(c) The Plan of Unification and the Price Paid by the City

Both Manhattan and Interborough have been in receivership since 1932. The Plan of Unification was the means of terminating the receivership by selling the properties of both companies to the City of New York for operation by it. The Plan refers to the Committees representing the first mortgage issues of each company as the "Contracting Committees".

"The Plan provided that on conveyance of the properties to the City it would pay over to the Contracting Committees some $151,000,000 of its Corporate Stock and would recognize certain cash adjustments which would bring the total price to about $164,000,000",* said the Circuit Court of Appeals in its opinion (R. 957, see also Plan provisions, R. 91, 94, 96-7, 104-5). Under the Plan, the entire $164,000,000 was available for distribution to the security holders of the two companies (subject to deduction for payments to their agents and attorneys, R. 98-9) as the City agreed to pay all claims made and taxes assessed against the two companies other than the claims of security holders (R. 118-125).

It is also, perhaps, worth emphasizing that the City bought the properties, not the Manhattan and Interborough securities, for the reason that our opponents have asserted below that the City was buying securities. This assertion is belied by the terms of the Plan (R. 85-8, 91) and the manner in which it was consummated (R. 45-6, 456-556). If further proof of the inaccuracy of such assertion be necessary, we respectfully refer the Court to the provi-

* Actually, the City paid about $20,000,000 in cash pursuant to its option and $144,000,000 in Corporate Stock (R. 462, 523, 560).

sions of the Plan giving the City options, never exercised, to buy the securities (R. 140-1).

(d) Treatment of Assenters to the Plan

The Contracting Committees were directed by the Plan to make offers at prices fixed by the Plan to all the security holders of each company, which offers, if accepted by all, would have exactly eaten up the $164,000,000.

$500 per Bond was the Plan price for Manhattan Second Mortgage Bonds against a total claim for principal and interest of $1,261.22 per Bond on the date of the consummation of the Plan, and the offers to that issue at the Plan price aggregated $2,261,500 (R. 154). The offers at the Plan price made to the holders of the $40,670,000 in principal amount of Manhattan Consolidated Mortgage 4% Bonds aggregated $36,551,663.39, paid to the extent of $19,902,750 in New York City 3% Corporate Stock, and amounted to approximately $900 per Bond against a total claim for principal and interest on the date of consummation of the Plan of about $1,100 (R. 46, 154, 462, 104-5). The aggregate of the offers at the Plan price made to the holders of the 600,000 shares of Manhattan stock was $12,096,160 in the form of Corporate Stock (R. 154). Thus the aggregate of the offers to assenting Manhattan security holders totalled $50,909,323.39, a sum more than the $50,760,000 necessary to pay all the Manhattan bonds in full with accrued interest to the date of consummation of the Plan (R. 154). The rest of the $164,000,000 was divided among the Interborough security holders.

These Plan prices for assenters were fixed for the most part by negotiations between committees representing various issues of securities (R. 579-82). The $500 price for Manhattan Second Mortgage Bonds was, however, fixed by negotiations between Mr. Cuthell, Special Counsel for the Transit Commission, and the Rockefeller interests, who owned over 60% of the issue when the Plan was signed (R. 316, 581, 593). Throughout the proceedings, the

Rockefellers steadfastly contended, through their representative, Curtiss, Belknap & Webb, that they did not represent the entire issue (R. 316, 593, 91, 146, 454), presumably because of their large ownership of other issues whose interests conflicted with those of the Manhattan Second Mortgage Bonds.

(e) Provisions for Non-Assenters to the Plan

The Plan did not purport to force security holders to accept the offers available for assenters. Instead, it provided that non-assenters would receive "the cash distributive shares to which all holders of securities shall be legally entitled" (R. 102). The amounts of these legal cash distributive shares were to be fixed by judicial sales and the Settlement Fund hereinafter described. Cash for non-assenters was to be provided by the City's buying back the Corporate Stock not taken down by assenters, at par if necessary (R. 102).

(f) Analysis of Plan

Reduced to its simplest terms, the Plan was one of liquidation involving a purchase by the City for $164,000,000 in cash and Corporate Stock of all the assets of Manhattan and Interborough in order that the City might operate the elevated and subway trains. With these proceeds, the two companies, through the agency of the Contracting Committees, were to offer to buy in their own securities for cancellation at specified prices. Those security holders who did not accept the offers were to receive their legal cash distributive shares. Where the cash was to come from if the sum of the legal cash distributive shares of non-assenters exceeded the cash and par value of the Corporate Stock available for them had they assented, does not appear in the Plan.

(g) Action of the District Court

By an order dated March 15, 1940, the District Court approved as fair the Plan prices offered assenters to the Plan (R. 419).

The Plan prices were all compromises of the maximum claims of each security to the $164,000,000 fund (R. 153-5). Had all security holders been forced to accept these Plan prices, the District Court would have had to pass on them; but since the only persons affected by the District Court's approval of the Plan prices were those who voluntarily accepted them, it does not seem to us that it had to pass on these prices at all any more than it would have had to pass on the fairness of any other compromise assented to by all persons affected.

The District Court's desire to pass on the Plan prices seems to have arisen from applying the technique applicable in reorganizations to a liquidation. When a court permits reorganization to take place in lieu of liquidation, it assumes that it is either advantageous or necessary for the same security holders to continue to operate the enterprise, and no real liquidation sale to an outsider is made. The proceeding which fixes the legal rights, the judicial sale, is likely to be of little value to any security holder since the upset prices fixed are based on a guess as to what liquidation might have realized, and, in practice, the guess is often influenced by lack of cash sufficient to make large cash payments to dissenting security holders and still continue to run the enterprise properly. The real opportunity for the security holders is furnished by the provisions made for them under the plan of reorganization, and hence the fairness of such provisions is of paramount importance.

But the Plan of Unification is a plan of liquidation. On the sale of the assets of Manhattan, each security holder was entitled to receive his legal share of the proceeds of the liquidation sale and this the Plan purports to assure him if he does not assent to it (R. 102). That he is also offered a chance to assent to the Plan and sell his securities for a compromise price need concern the courts no more than the price at which his securities might be selling

on the market, and certainly should not, in theory, affect the size of his legal cash distributive share in the proceeds of the liquidation sale.

It is earnestly contended that *Consolidated Rock Products Co.* v. *Du Bois,* 312 U. S. 510, and *First Nat. Bank* v. *Flershem,* 290 U. S. 504, required the determination of the legal rights of non-assenters by means of allocating, with the aid of independent appraisers, part of the $164,000,000 purchase price to the Manhattan properties, the remainder to the Interborough properties, and thereafter determining the amount and ownership as between Manhattan and its stockholders of the admittedly enormous claims against Interborough in favor of Manhattan parties arising out of the 1903 Lease. If not valued at par, the $144,000,000 of Corporate Stock contained in the $164,000,000 purchase price should certainly have been valued at some figure no lower than the lowest sales price paid in 1940 for it or any comparable New York City issue, which price was 88⅛* on a "when issued" basis.

So much for theory. In practice, the District Court did approve all the Plan prices on March 15, 1940 (R. 419). In practice, this approval was not based on any allocation of the $164,000,000 purchase price to the respective properties of the two companies with the aid of independent appraisers or on any other fundamental determinations with respect to rights under the Manhattan Lease. In practice, this approval of the Plan prices has determined the legal cash distributive share of each issue of Manhattan securities because these shares were actually fixed by taking 80% of their Plan prices (R. 888-91).

The procedure pursuant to which the legal cash distributive shares of various classes of non-assenters was fixed

* This low figure was the result of the issuance by the City of New York of almost $300,000,000 in principal amount of 3% Corporate Stock in June of 1940 at a time when France was being overrun. The 1941 range is 100 - 111⅝; the 1940 range 88⅛ - 104⅛.

was not even intended to determine their legal shares in the $164,000,000 some of which would necessarily have been greater and others smaller than the assenters' shares in the same fund. In the words of the Circuit Court of Appeals: "It may be conceded that the procedure adopted was intended to make assent to the Plan more attractive than dissent" (R. 957). How well it succeeded can be seen by reference to the following table:

Issue	Assenter's* Plan Price Per Unit	Non-Assenter's Cash Distributive Share Per Unit	Total* Payable to Issue if all Holders Assented (Sum of Plan Prices)	Total Payable to Issue if No Holders Assented (Sum of Distributive Shares)
Man. Con. Mortg. 4% Bonds, $1,000 Principal Amount	$898.74	$729.44	$ 36,551,663.39	$29,666,666.67
Second Mortg. 4% Bonds $1,000 Principal Amount	500.00	394.68	2,261,500.00	1,785,133.73
Man. Guaranteed 7% Stock	35.00	27.63	1,522,850.00	1,202,073.40
Man. Modified Guaranteed 5% Stock	19.00	15.00	10,573,310.00	8,346,126.20
			$ 50,909,323.39	$41,000,000.00
Int. First Mortg. Bonds $1,000 Principal Amount	$848.74	$372.29	$ 82,493,063.47	
Int. Secured** 7% Notes, $875.99 Principal Amount	816.17	595.97	25,849,878.63	$56,000,000.00†
Int. Unsecured 6% Notes, $1,000 Principal Amount	350.00	81.77	3,675,000.00	
Int. Stock	3.00	0.00	1,050,000.00	0.00
			$163,977,265.49	$97,000,000.00

* Payable entirely or almost entirely in City Corporate Stock except for the Manhattan Consolidated Mortgage 4% Bond Issue which was payable 45% in cash, 55% in Corporate Stock (R. 485-99).

** Each Note was secured by about $1,736.00 in principal amount of Interborough First Mortgage Bonds.

† $6,000,000 represented the proceeds of unmortgaged property.

1. The Foreclosure Sales

The first step in fixing the legal cash distributive shares of non-assenters was to sell at foreclosure on January 25, 1940 the Manhattan physical properties (but not $6,000,000 in cash and the claims on the Lease against Interborough, R. 240) for $17,000,000 to the Merle-Smith Committee representing the assenting Manhattan Consolidated Mortgage Bonds (R. 678). Then the Interborough properties were sold at a judicial sale to the Morgan Committee representing the assenting Interborough bonds for $56,000,000, subject to the claims of the Manhattan parties on the Lease (R. 894, 747-8, Exhibit 52, Vol. VII, pp. 33-35). It was later determined in a class action known as the Settlement Fund proceeding, that the Manhattan parties were owed $18,000,000 by the Interborough, and Manhattan non-assenters were permitted to share in this $18,000,000. Thus the funds on the basis of which non-assenters are now being paid total $97,000,000.

The Manhattan properties were sold at an upset price fixed by the District Court on the basis of testimony given that very day by a single expert called by the committee representing assenting Manhattan Consolidated Mortgage bondholders (R. 675, 647, 187, 219). The expert did not consider the $164,000,000 amount paid by the City for the properties of the two companies or the value of the Interborough properties (R. 647-75). To be sure that the assenters would not be injured by the sale, the foreclosure decree contained provisions permitting the District Court to void the sales in the event that the Plan was not approved (R. 217-8).

On June 12, 1940, the purchasing committees acquired title to the properties of the two companies (R. 241-304) and on the same day they conveyed them to the City of New York (R. 524-556) in return for its promise to pay some $14,000,000 in cash and $144,000,000 in Corporate Stock (R. 527, 539, 560, 91, 94, 96-97, 104-5), some $6,000,000

in cash being paid by the Manhattan Consolidated Mortgage Trustee directly to holders of Manhattan Consolidated Mortgage Bonds (R. 96-7). The effect of these transactions has been to solemnly adjudge that, although the City has always been willing to pay about $164,000,000 for all the properties, the legal rights of the security holders in the proceeds of the properties totaled only $97,000,000 or that the $144,000,000 of Corporate Stock was worth only 51, 37 points less than the lowest price at which this issue of municipal bonds has ever sold.

Of course, the foregoing does not by itself prove that the Manhattan foreclosure price was too small a portion of the $164,000,000 paid by the City, but the rest of the Record does. To mention a few salient points, the assessed value of the Manhattan railways and the power plant alone at the time of foreclosure was $42,600,000 (R. 878), a fact which the Manhattan expert did not have before him (R. 878). It is true that the earnings of the Manhattan railways were bad, but the City wanted them to tear them down, not to operate them for any length of time, and in fact tore down roughly half of them in 1940. The only other method of acquiring the lines open to the City was by condemnation and in condemnation proceedings, the City would have had to pay at least the assessed value fixed by the City itself. The Sixth Avenue line alone was condemned in 1938 for $12,500,000 (R. 590) and the trackage transferred to the City in 1940 was about five times that of the Sixth Avenue line. The Manhattan rolling stock and power plant was valued at from $8,000,000 to $10,000,000 by the assenters' own expert (R. 654, 772).

On the other hand, the experts used on the Interborough foreclosure testified that the upset price should be $40,000,000 for the Interborough mortgaged properties (subject to claims later compromised for $18,000,000) and $6,000,000 for the Interborough unmortgaged properties (R. 722, 740). After hearing argument of counsel, the

District Court raised the upset price on the foreclosed assets to $50,000,000 (R. 748). Nothing in the Record, then, indicates that many of the missing millions should be allocated to the Interborough properties.

2. The Settlement Fund

Throughout the proceedings, the holders of all of, Manhattan 600,000 outstanding shares claimed that they had obtained in 1903 a direct assignment to themselves of rent payable by Interborough under the Lease of all the Manhattan assets, to the extent of $7 a year per share. The holders of the 556,490 shares whose owners accepted the Modified Guaranteed status in 1922 limiting them to payments of $5 a year payable only if earned by either Manhattan or Interborough thereafter, further contended that they had been restored to a position where they had a claim of some $57 a share as creditors of Interborough, by reason of the failure of Interborough to pay a disputed claim of $5.50 a share for dividend rental asserted to have been earned in 1928, 1929 and 1930 (R. 809-824, 840-6).

It is impossible to discuss adequately, within the bounds of this petition, the merits of the contention of any class of Manhattan stockholders that they were direct creditors of Interborough. Suffice it to say here that the language of the Lease (Exhibit A, attached hereto) requires Manhattan to declare dividends before its stockholders are to receive the $7 annual payment and that it merely gives Interborough the privilege of paying the stockholders of Manhattan directly, the "dividend rental" being payable to Manhattan. Perhaps it is worthwhile to point out that Manhattan had outstanding in 1903 $40,000,000 in bonds (Exhibit 4, Vol. III, p. 12) and provided in the Lease itself for the subsequent issuance of the Manhattan Second Mortgage Bonds (Exhibit 4, pp. 8, 12), and that the Lease made no provision for paying principal on any bonds (Exhibit 4, p. 13). Since the Manhattan stock was $100 par

value stock (Exhibit 4, pp. 4-5), the assignment of rent to the stockholders would have been an illegal dividend or distribution to stockholders, impairing capital under New York law (§ 23, Chap. 354, N. Y. Laws of 1901). Thus it would appear that any claims for rent, including the "dividend rentals", belonged to Manhattan Company and through it to its creditors.

Since the above described controversy existed as to what part of the claims for rent belonged to the Manhattan Company and were, as a result, subject to the Manhattan Consolidated Mortgage, none of these claims were sold at the Manhattan judicial sales (R. 240). Thus, even after the sale of the Manhattan physical assets for $17,000,000, the Manhattan non-assenters had these claims on which to realize. In fact, the Manhattan non-assenters were the sole parties interested as plaintiffs in a determination of the value and ownership of these claims as all Manhattan assenters, by assenting, specifically agreed to sell their securities at the Plan prices and to give up their right to share in the proceeds of these claims (R. 103-4, 114). Besides the assenters and their committees had an adverse interest to that of the non-assenters since, if there should not be enough of the $164,000,000 left after the distribution to assenters to take care of non-assenters, those assenters who received too much and those responsible for the excessive distribution would undoubtedly be liable to non-assenters. Until June of 1940, the City had not agreed to assume any such liability (R. 102, 528-9, 532-4, 549, 553-4).

Despite the adverse interests of the assenters, the committee representing assenting Manhattan Consolidated Mortgages brought*, on behalf of all Manhattan non-

* The Circuit Court of Appeals stated (R. 956) that the Trustee for the Manhattan Second Mortgage Bonds had started the suit but all it did was to file a proof of claim against the Interborough in 1938 before the Plan was formulated, which proof of claim was adopted by the committees representing assenters as one of their pleadings (R. 344-5, 354).

assenters, class actions to have all matters in connection with the claims on the Manhattan Lease determined (R. 335-57). A few days later, the assenters, pretending to represent the non-assenters under Rule 23 of the Federal Rules of Civil Procedure, compromised the class actions by the Settlement Fund Order, an order entered on March 15, 1940, the same day that the Plan prices were approved (R. 410-9). The Settlement Fund Order raised the amount of the $13,500,000 Fund originally proposed (R. 396-9)) to $18,000,000 as a result of oral argument (R. 888-91). If one adds $18,000,000 to the $6,000,000 in cash in the hands of the Manhattan Consolidated Mortgage Trustee (R. 673-4) and the $17,000,000 Manhattan foreclosure price, one gets $41,000,000, not the fund of the value of approximately $51,000,000 which the Interborough parties were willing to let the Manhattan parties have (R. 154) and the City was originally willing to pay to Manhattan assenters and non-assenters combined (R. 102).

But even $41,000,000 would have been sufficient to pay on March 15, 1940, all non-assenting Manhattan bondholders in full and all assenting Manhattan bondholders their Plan price (see table at page 12 herein, third column, and R. 403). To make certain that no non-assenting Manhattan bondholder would receive more than he would by assenting, the Manhattan non-assenters were not allowed to fight over the allocation of the $18,000,000. Instead the Settlement Fund was arbitrarily allocated by the Settlement Fund Order so that each Manhattan non-assenter would receive approximately 80% of what he would get by assenting, the non-assenting Manhattan Second Mortgage Bonds receiving $394.68 and the non-assenting Manhattan stockholders over $9,500,000 or an average of $16 a share (R. 888-91). Not a single non-assenting Manhattan security holder, any representative of his, any receiver or mortgage trustee agreed to compromise all the claims at $18,000,000 or to allocate the $18,000,000 on the 80% basis. That no Manhattan non-assenter would agree to such a compromise would seem to be obvious since a better com-

promise was available from March 15, 1940 to September 26, 1940 by assenting to the Plan (R. 564-5). The assenters took care to prevent the Settlement Fund Order from affecting them by providing therein that if the Plan was not consummated, the compromise provided for would be null and void (R. 418).

This compromise is justified by the proponents of the Plan because representatives of the petitioner were in Court, objecting to the compromise. Even assuming that the compromise was a fair one, it would seem that a class of plaintiffs, just like an individual plaintiff, should have a right to refuse any compromise in favor of taking its chances on the outcome of the litigation.

Nor is there any indication that the compromise of $394.68 per Bond was fair. Although there was considerable evidence before the District Court, no possible relationship between this evidence and the result achieved has ever been shown. The correctness of the contention that any of the Manhattan stockholders were entitled to be paid as creditors of Interborough was never decided (R. 400-9, 960), and there is no discussion anywhere as to the means by which the Modified Guaranteed Stock expanded a possible claim of $5.50 a share into a payment of $15.00 a share (R. 564). Even assuming the basic contention of the Manhattan stockholders to be correct, until it is also decided how much of the $18,000,000 was paid on account of Interborough's failure to pay, as rent under the 1903 Lease, interest on Manhattan bonds, $9,000,000 in taxes payable by Interborough under the Lease but paid by the Manhattan Consolidated Mortgage Trustee (R. 204-5, Exhibit 4, pp. 15-6), the "dividend rental" of the Guaranteed Stock and the "dividend rental" of the Modified Guaranteed Stock, respectively, and until it is determined how much of the $164,000,000 paid by the City for the properties of the two companies should be attributed to the purchase of Manhattan properties, there is no criterion for determining the fairness of the allocation of the $18,000,000.

All in all, this case is as much like *Consolidated Rock Products Co.* v. *Du Bois,* 312 U. S. 510, as a liquidation can be. The temptation to come to an arbitrary result because the situation was complicated was not resisted by the District Court in either case. This is especially unfortunate for the Manhattan Second Mortgage Bonds since the issue is so small that a very little change in the valuations or allocations makes a great change in the amount to which they are entitled, and a decision in their favor on any one of a number of undecided issues would entitle them to payment in full.

(h) Opinion of the District Court

The opinion of the District Court has nothing to say with respect to the legal rights of the non-assenters, merely concluding that the Plan seemed fair for assenters (R. 405-6). If it was, it was difficult to see how the compromise at a 25% discount forced on Manhattan non-assenters was also fair, to say nothing of the treatment accorded to Interborough non-assenters (see table at page 12 hereof).

(i) Proceedings in the Circuit Court of Appeals

Appeals were taken to the Circuit Court of Appeals from virtually all the orders and decrees in the District Court in order to avoid procedural difficulties. Argument was had in the Circuit Court on May 22, 1941.

(j) Opinion of the Circuit Court of Appeals

The opinion of the Circuit Court of Appeals said that no doubt was cast upon the $97,000,000 basis on which the legal cash distributive shares of non-assenters was fixed because the $164,000,000 price paid by the City was paid partly in Corporate Stock (R. 957-8). It did not discuss the value of the Corporate Stock. It cites as support certain reorganization cases (R. 958) in the lower Federal courts (all decided before this Court's decision in *First Nat. Bank* v. *Flershem,* 290 U. S. 504) which upheld low

upset prices as a necessary device to keep the old security holders in control of the reorganized enterprises. It is respectfully suggested that the old security holders here do not now control the City of New York because of their ownership of New York City Corporate Stock, and through it the transit facilities.

We reiterate that this case involves a liquidation. Hence no question arises as to keeping the old security holders in control of the enterprise as they are all abandoning it. Hence there is no need to guess at the fund available for distribution on liquidation for it is the sum paid by the outside purchaser, the City. In a liquidation, the Court has no concern over preserving cash necessary to keep the enterprise running for that problem is one belonging to the outside purchaser. There can only be a cash shortage in the fund to be distributed and it can only arise if some security holders take more out of the fund than they are entitled to. Even if, as was the case here, the majority of the security holders wish to turn in their securities for fixed compromise prices, there still should be cash to pay those who wait to have their legal rights determined unless the other security holders have taken too much. Such a contingency may easily be guarded against by an appropriate reserve out of the compromise prices or by having the outside purchaser, as the City eventually did here in effect, agree to put up any funds needed to pay the legal cash distributive shares of non-assenters (R. 528-9, 532-4, 549, 553-4). Nor is any special difficulty caused by the payment in Corporate Stock, since it could easily be turned into cash, either by sale on the market or by resale to the City in accordance with the Plan (R. 102); and such a course was not even necessary as the petitioner, like the assenters, has always expressed his willingness to be paid in Corporate Stock (R. 328).

It is also suggested that the error in the Circuit Court's argument may be seen by considering the situation as it would have been had the City exercised its option to pay

all in cash (R. 107). Then the small cash distributive shares could not have been justified on the ground that they forced the security holders to take their Plan prices in securities. Nevertheless, it is submitted that the exercise of that option would not have made the proceedings any more or less a liquidation than the payment partly in Corporate Stock. Manhattan was not in the business of running an investment trust of municipal bonds, it was a railroad company. It took the Corporate Stock as a step in the winding up of its affairs, just as it might have taken United States Government Bonds or coal in payment for its assets, with a view to reselling them, if its security holders would have realized more from payment in those mediums in lieu of cash.

To summarize the matter, it is the petitioner's contention that on this liquidation, the price which must be deemed to have been paid for the assets of Manhattan is the price actually obtained for them from the outside purchaser, that is the Manhattan share of the $164,000,000 in cash and Corporate Stock. Surely, this must be the "proper price" under *First Nat. Bank* v. *Flershem,* 290 U. S. 504, page 526. To deprive the petitioner and those he represents of his share in the $164,000,000 by means of intermediate judicial sales which bring but $97,000,000 is to apply the technique evolved to make reorganization possible where liquidation is inadvisable to a situation where liquidation is deemed advisable by all and actually takes place.

The Circuit Court also stated that in its opinion the $18,000,000 total of the Settlement Fund was adequate although it gave little reason for this conclusion (R. 956-7). It gave no reasons in support of the allocation of the $18,000,000 as between the various issues of Manhattan securities and in particular for the amount of the allocation of over $9,500,000 to the Manhattan stockholders, other than their claim under the Manhattan Lease that

they were entitled to be paid something as creditors of Interborough (R. 959). It did not even decide that this claim of the Manhattan stockholders was valid (R. 960). It seems to set forth the doctrine that if one has a class claim it may be compromised, after notice and a full hearing, without the consent of any member of the class or representatives of the class, because some members of the class are in court protesting that they do not want to compromise on the basis suggested (R. 956-7); in other words, that a class of plaintiffs, unlike a single plaintiff, may be forced under Rule 23 (c) of the Federal Rules of Civil Procedure to accept a compromise against its will, if the compromise is thought fair by the defendants and the court. If the opinion does not mean what has just been said, it must mean that the assenters, who were entitled to their Plan prices and only their Plan prices regardless of the outcome of the class actions (R. 103-4), were persons "as will fairly insure the adequate representations" of the non-assenters under Rule 23 (a), in consenting to a compromise of a class action on behalf of the non-assenters. The propriety of this compromise is especially difficult to understand because the assenters making it obtained for the non-assenters they purported to represent only 80% of what they themselves were already entitled to receive; and the non-assenters could obtain for themselves, if they had been in a compromising mood, the better compromise already accepted by the assenters through the simple expedient of assenting during the ensuing six months (R. 562-5).

The Circuit Court also quotes from an opinion of this Court, dealing with a statutory reorganization, asserting the desirability of resolving conflicting claims to specific assets by compromise (R. 957). Can it not be assumed that the compromises referred to by this Court were compromises made on behalf of an entire issue of securities by persons who had an interest in seeing to it that the compromise was as favorable as possible to that issue and

not, as was the case here, compromises made on behalf of some of the security holders by others whose slight interest in the controversy being compromised was adverse to those they purported to represent.

The Circuit Court of Appeals seems to have had a feeling that the City of New York had a special power in these proceedings to affect legal rights (R. 953, 961). The City was, of course, the highest and only real bidder for the properties of the two companies on liquidation and, if it had not bid, all the security holders might well have fared worse; but clearly that fact alone did not give the City the power to change the ordinary priorities in the purchase price of the stockholders and creditors of the sellers. In the decision in *Murray* v. *Roberts*, 103 F. (2d) 889 which reversed the decision of the District Court permitting the Interborough receiver to disaffirm the Manhattan Lease, the Circuit Court held in effect that the Lease could not be disaffirmed unless the Manhattan and the City consented (see opinion, pp. 897-8). As a practical matter the City might have had the power to force a change in the terms of the Manhattan Lease and it could have used the possible existence of this power as a club to force Manhattan parties to accept a low, separate price for the Manhattan properties and their claims against Interborough. The City, however, offered a lump sum of $164,000,000 for both properties and did not buy the Manhattan claims against Interborough at all, and in doing so, stated that it did not care how the purchase price was allocated (R. 580-1). So long as the City kept this $164,000,000 offer alive, any change in the terms of the Lease, had one been made, would merely have enriched the Interborough parties at the expense of the Manhattan parties and would have gained the City nothing. Surely the unexercised power to make such a change did not make the legal rights of anyone in the $164,000,000 so indefinite that they could be fixed by simply taking 80% of the negotiated compromise Plan prices.

(k) The Petitioner's Position

The petitioner has never objected to the sale of the Manhattan and Interborough properties to the City for $164,000,000; he merely objects to the allocation of the proceeds (R. 319-29). The City of New York stood ready under the Plan to pay at least $500 in cash for each Bond represented by the petitioner (R. 102), and, since June 12, 1940, to indemnify any other person liable for the dissipation of any portion of the $164,000,000 fund to which the petitioner is legally entitled (R. 528-9, 532-4, 549, 553-4). Hence, a successful appeal would merely require payments by the City greater than the $394.68 now reserved for each of the 484 bonds, it would not necessitate the return of the properties to the companies or even additional payments to assenters. *First Nat. Bank* v. *Flershem,* 290 U. S. 504, 521. In a very real sense, this is nothing but a condemnation proceeding brought by the City against the petitioner's bonds.

The opportunity for holders of Manhattan Second Mortgage Bonds to assent and receive $500 in Corporate Stock expired on September 26, 1940 (R. 564-5). At that time, petitioner had the choice of either taking the $500 per Bond or, by prosecuting his appeal, seeking to have his legal rights really determined. The petitioner chose the latter course, although it involved the risk of receiving only $394.68 per Bond. After all, petitioner held Bonds in a company all of whose assets had been sold for proceeds distributed in large part to stockholders. He had always supposed that in such a liquidation the burden of showing why his Bonds should not be paid in full rested on his corporation and those who stood in its stead. He further felt that no reason had been shown to justify giving up 60% of his claim. It seemed unlikely to him that any appellate court would hold that negotiators, who had accepted for themselves and themselves only, a compromise of $500 per Bond on which $1,261.22 was due, could force him to accept over his objection a compromise of $394.68

per Bond, without having any of the valuation questions decided on the basis of what the City was paying or the legal questions decided at all.

Specification of Errors to be Urged.

1. The Circuit Court of Appeals erred in affirming the decision of the District Court that the legal cash distributive share to which non-assenting Manhattan Second Mortgage Bondholders were entitled on the liquidation of their company was $394.68.

2. The Circuit Court of Appeals erred in not entering an order directing that the non-assenting holders of Manhattan Second Mortgage Bonds should receive (1) payment in full on the basis of the existing Record, or (2) a new trial to ascertain what amount in excess of $394.68 per Bond is their legal distributive share, or (3) $500 in Corporate Stock, the treatment accorded to assenting holders of Manhattan Second Mortgage Bonds.

The Reasons Relied on for the Allowance of the Writ.

I. The Circuit Court of Appeals has decided several important questions of Federal law which have not been but should be settled by this Court as they will be of great importance in connection with plans for geographic integration and corporate simplication under Section 11 of the Public Utility Holding Company Act of 1935 and in connection with plans for liquidating corporations under the Bankruptcy Act. These questions are:

A. That on the liquidation of corporations by the sale of their assets for a fund of securities and cash having a value of approximately $164,000,000, the legal rights of security holders in the fund may be determined as if the assets had been sold for $97,000,000 in cash.

B. Either that under Rule 23(a) of the Federal Rules of Civil Procedure, those who have irrevocably accepted an offer on the liquidation of their corporation to sell their securities at a definite price are persons "as will fairly insure the adequate representation of all" other owners of the same issue of securities who have refused to accept that offer, in a class action brought to determine what those who refused the offer are legally entitled to receive; or that under said Rule 23(c), a compromise of a class action may be approved by the District Court even if no member or representative of the plaintiff class assents to the compromise, as long as some member of the class is in court objecting to the compromise.

C. Either that the burden is on the creditors of a corporation to show why they are entitled to be paid in full on liquidation, even though stockholders receive large amounts of municipal bonds and cash; or, that on the liquidation of a corporation, the burden on the corporation of showing why its creditors should not be paid in full is satisfied where a claim can be made that the stockholders are entitled to be paid an indeterminate amount as creditors of another corporation, even though the correctness of that claim is not decided.

II. The Circuit Court of Appeals has decided several Federal questions in a way probably in conflict with applicable decisions of this Court.

A. The rights of the non-assenting Manhattan Second Mortgage Bondholders have been fixed by judicial sales of the assets of Manhattan and Interborough for $97,000,000 when the City of New York was bound to pay for the properties cash and Corporate Stock having a value of approximately $164,000,000. Thus it is apparent that these orders and decrees ignore the bid of the City of New York, there-

by violating the rule of *First Nat. Bank* v. *Flershem*, 290 U. S. 504, 526-8, requiring that upset prices be based on the best bid which might have been obtained.

B. It has decided, that on the liquidation of two jointly operated corporations by the sale of their properties for a single sum, the District Court may determine that a plan under which offers are made out of the proceeds of the sale to purchase the outstanding securities of the corporations for stated amounts is fair, without allocating the purchase price paid to the assets purchased or making the other fundamental determinations required by *Consolidated Rock Products Co.* v. *DuBois*, 312 U. S. 510; and that on the basis of such a decision as to fairness, the District Court may force those who do not accept these offers in order that they may appeal, to take 80% of the amount refused, still without making the determinations required by that case.

C. It has decided that the rule in equity receiverships that every important determination by the court calls for the exercise of an informed independent judgment laid down in *National Surety Co.* v. *Coriell*, 289 U. S. 426, 436 and in *First Nat. Bank* v. *Flershem*, *supra*, 525, does not apply where the receivership culminates in liquidation rather than reorganization.

III. In affirming the District Court, the Circuit Court of Appeals has sanctioned a departure from the usual course of procedure which seems to us to require an exercise of this Court's power of supervision. In connection with the liquidation of two jointly operated companies, the District Court has approved a negotiated compromise plan of liquidation for those who wished to assent to it, which compromise gave large sums to stockholders. It has done this without making the determinations required by *Consolidated Rock Products Co.* v. *Du Bois*, *supra*, if even a plan of reorganization is to be found fair and equitable. It has not compelled acceptance of the compromise

plan, it has offered each non-acceptor the alternative of obtaining their "legal rights" by means of judicial sales and class actions "intended to make assent to the Plan more attractive than dissent", to quote the Circuit Court of Appeals (R. 957). To get such a result, it necessarily had to determine "legal rights" not on the basis of the fund paid for the assets of the two companies but on a lesser amount, here less than two-thirds of the fund; and it did in fact give 10% of the two-thirds to the Manhattan stockholders, without making any findings which justify the amount of this allocation to stockholders or any allocation at all. It is respectfully urged that this procedure is wrong. If creditors are to be protected on a reorganization because of what their rights would have been on liquidation, they are entitled to at least as much protection where liquidation takes place. Failure of this Court to act will once more revive the hope that stockholders may recover at the expense of the corporation's creditors if only the proceedings are complicated enough to partially disguise what has happened.

Position of the Chase Bank.

Since Paul E. Manheim is not a party to the two Foreclosure Actions in the United States District Court for the Southern District of New York, in which orders were entered by said District Court and affirmed by the Order of the United States Circuit Court of Appeals for the Second Circuit sought to be reviewed, and since The Chase National Bank of the City of New York, as successor Trustee under the Second Mortgage and Deed of Trust of Manhattan Railway Company dated June 1, 1913, under which the bonds owned or represented by Paul E. Manheim are outstanding, is a party to said two Foreclosure Actions, The Chase National Bank of the City of New York, as such Trustee, hereby joins, at the request of Paul E.

Manheim, in the foregoing Petition, for the sole purpose of protecting the rights, if any, of Paul E. Manheim and of the holders of the said bonds.

WHEREFORE it is respectfully submitted that this petition for a Writ of Certiorari to the Circuit Court of Appeals for the Second Circuit should be granted.

Dated, New York, N. Y., December 17, 1941.

LOUIS CONNICK
Counsel for Petitioner Manheim

HUGH L. M. COLE
Counsel for Petitioner
The Chase National Bank
of the City of New York

Exhibit A.

Excerpt from the Manhattan Lease (Exhibit 4, Vol. III).

"ARTICLE SIXTH.—The Lessee hereby leases and hires from the Lessor the said railroad and railroads, franchises, rights, privileges, easements, real estate and property, hereinbefore mentioned, described and demised, for and during said term of nine hundred and ninety-nine years aforesaid, and upon the terms and conditions of this lease expressed, and the Lessee hereby covenants and agrees to pay to the Lessor and hereby guarantees to each owner of record of shares of capital stock of the Lessor, dividends, as rent, as hereinafter provided, for the term of two years and nine months from the 31st day of March, 1903. The Lessor hereby covenants and agrees, that prior to the date of payment of each of the instalments of rent provided for in this article, it will declare a dividend equal to such instalment, payable upon the date of payment of such instalment, * * *.

* * * * * * * *

No reduction of the guaranteed annual dividend rental or in the terms of years of this lease shall be made without the unanimous consent of the shareholders of record of the Lessor; provided, however, that nothing herein contained shall otherwise limit the lawful powers of the Board of Directors and shareholders of the Lessor to deal with the subject-matter of this lease and its provisions.

From and after the expiration of said two years and nine months, and from January first, 1906, the Lessee hereby covenants and agrees to pay to the Lessor, and guarantees to each owner of record of the shares of capital stock of the Lessor, as rent, an annual dividend of seven per centum (7%) of his holding of the capital stock of the Lessor.

The Lessee hereby covenants and agrees that it will each and every year during the term hereby granted, beginning with the first day of April, 1903, pay to the Lessor as rent for the demised property, and hereby guarantees to the respective owners of record of the shares of the Lessor, the said annual dividends free

of all charges, in quarter-yearly payments * * *; and the Lessee will from time to time execute in proper form a guarantee to the above effect, printed or engraved upon the certificates of stock of the Lessor; * * *.

The form of such Guarantee shall be as follows:

'Dividends amounting to six per cent. per annum and an additional amount, if earned, not exceeding one per cent. per annum, until January first, 1906, and after that date, dividends amounting to seven (7) per cent. per annum, upon the par value of the outstanding capital stock of the Manhattan Railway Company are guaranteed, and will be paid by the undersigned, in accordance with the terms and provisions of a certain Indenture made between the Manhattan Railway Company and the undersigned, dated the first day of January, 1903.

INTERBOROUGH RAPID TRANSIT COMPANY;
By Treasurer.'

Payment of dividends as above provided by the Lessee to the stockholders of the Lessor shall constitute payment of rent, in compliance with the foregoing covenants to pay the same to the Lessor."